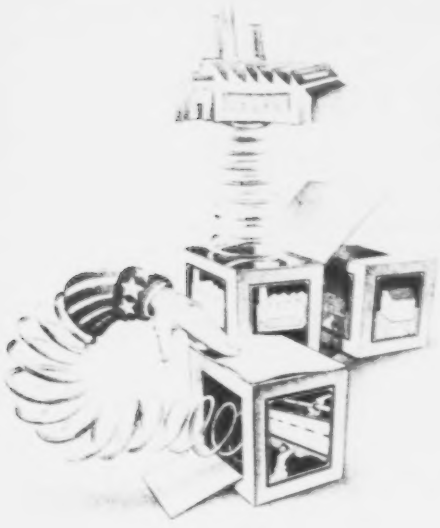
1982 Dodge/Sweet's Construction Outlook

First Update
March 1982



New Priorities for Construction

The shaky start of the Reagan Administration's Program For Economic Recovery calls for some modification of last October's *1982 Construction Outlook*. These changes do not affect the bottom line so much as they alter the character of 1982's potential for construction contracting and building materials demand.

One of the necessary adjustments to the *1982 Outlook* is a downward revision of the housing forecast, from 1.4 million units to the range of 1.2 to 1.3 million. This shortfall became evident early in the winter when interest rates firmed unexpectedly.

Not long after that, the release of 1981's fourth quarter GNP data, which revealed a sharp decline in economic activity, confirmed the suspicion that another recession was in the making. In deference to an embarrassed Administration, which had been pushing growth, the consensus economic forecast for 1982 initially took the form of a "mild recession/strong recovery" scenario. By February, however, this deferential outlook was rapidly losing whatever credibility it once had. The reality of a more severe recession now demands downscaling 1982's potential for commercial and industrial building. At the same time, it improves the odds on reaching the upper limit of the 1.2 to 1.3 million unit housing forecast.

Caught in the Cross Fire

For most of the past year, the construction industry has been caught in the cross fire of a grim battle against inflation. Both the Administration and the Federal Reserve Board—each in its own way—insist they are winning the battle. Construction has been one of the casualties.

Part of the problem concerns the inherent conflict between the supply-side and monetarist approaches to the control of inflation. The simultaneous application of monetary *restraint* and budgetary *stimulus* has the Fed blaming the Administration for inflation while the Administration is blaming the Fed for recession. And that's only the up-front part. In the background lurk the promise of further tax cuts and the dedication to a budget-busting military buildup.

Until these priority conflicts are resolved, the short-run consequences of the first year of Reaganomics—recession, high interest rates, and across-the-board cuts in non-defense spending—have the construction industry pinned down on all sides. In 1982, as in 1981, housing can't recover until interest rates break. Publicly financed construction faces a long wait until local governments are capable of accepting the responsibilities of the New Federalism. Meanwhile, private nonresidential building, where the best potential lies, is sitting out the recession of 1981/82.

It is extremely rare to find all three sectors of the construction market suppressed at the same time. More often than not, cycles in *non*residential building, which are dominated by business capital spending, move in opposite phase from housing cycles, which are highly sensitive to credit conditions. This tendency toward counter-cyclical behavior of nonresidential and residential building activity usually serves as a stabilizing influence in construction markets.

Under ordinary circumstances, the balance of 1982 would find construction markets settling into a familiar pattern. Recession, now almost three quarters along, would be dragging commercial and industrial building into further decline, just as it did in 1970 and again in 1975. Falling interest rates would be the catalyst for a vigorous housing recovery, particularly with the support of today's highly favorable demographics. Depending on the severity of the recession, it would not be surprising to find the Federal government providing the stimulus of some extra public works construction as it has so often done. By this sequence of events, construction has typically led the economy out of past recessions.

But these are not ordinary times. Among these familiar responses by construction to recession, only one, the weakening of commercial and industrial building, carries a high probability in

1982. The likelihood of increased public works spending this year is close to zero, because this Administration remains committed to tax cuts and military spending as the way to stimulate the next recovery. This leaves the demoralized housing industry as the main chance for short-run improvement in the depressed construction markets.

Residential Building

Since the fall of 1979, when the Fed "officially" embraced monetarism, the hopes of the housing industry have fallen and risen with swings in interest rates. Mostly, it's been high interest rates and low housing volume. What happened during the brief period of monetary relaxation in the second half of 1980, however, proved that housing's response to falling interest rates can be swift and strong. Housing improved nearly 50 percent during that six-month period. Another round of credit tightening at the close of 1980 ended that spurt, but by the fall of 1981, as interest rates began to wind down again, there was reason to anticipate another housing rebound. It failed to materialize, however. By midwinter, interest rates were defying the law of gravity—rising instead of falling, even though the economy was limping its way through another recession. The monetarist explanation for this curious happening is that M-1 escaped again and had to be recaptured, even at the cost of deepening and lengthening the recession.

It must be hoped that the $10 billion "mystery bulge" that appeared in the money supply in January, prompting the Fed to tighten when it might have been easing, was a random event. If so, the unpleasant realities of recession should prevail in the credit markets over the months ahead, and interest rates will resume their downward course as business demand for borrowing slackens. Even so, the recent flare-up of interest rates, though short-lived, has already diminished the prospect for a housing recovery. In 1982, the Federal government will be skimming as much as one third of the available credit, mostly to finance its huge deficit. Business demand for funds should increase toward year-end as recovery finally takes hold. This leaves the housing market only a few precious quarters in which to revive.

Allowing for the usual lag between short and long-term interest rates, prime time for mortgaging ought to be from spring 1982 until the end of the year. During this period, conventional mortgage rates are expected to retreat from their present 17+ percent to about 14 percent. With inflation at 8 percent, the "real" rate of interest on conventional mortgages would still be a relatively high 6 percent, providing one reason why the nominal mortgage rate can remain fairly steady at 14 percent rather than surge again next winter.

Fourteen percent mortgage money is not the stuff that housing booms are made of, but it should provide an environment in which "innovative" financing works better than it does at 17 percent. While it appears that the bottom of the current housing cycle has been reached, there can be little hope for anything better than a rate of 1.0 million starts in 1982's first quarter. Modest improvement, to 1.2 million in the second quarter, followed by rates of 1.4+ million and 1.5+ million in the third and fourth quarters, will be needed to reach 1.3 million for the year. The final quarter is apt to be the critical one.

1982 National Estimates
Dodge Construction Potentials

First Update
March 1982

	Nonresidential Buildings	1981 Actual	1982 Forecast	Percent Change 1982/81
Floor Area (millions of square feet)	Office Buildings	317		–21
	Stores & Other Commercial	404		–6
	Manufacturing Buildings	185		–8
	Total Commercial & Manufacturing	906		–12
	Educational	74		–12
	Hospital & Health	60		–8
	Other Nonresidential Buildings	126		–5
	Total Institutional & Other	260		–8
	Total Nonresidential Buildings	1,166		–11
Contract Value (millions of dollars)	Office Buildings	$ 19,268		–15
	Stores & Other Commercial	11,733		+ 2
	Manufacturing Buildings	7,530		+28
	Total Commercial & Manufacturing	$ 38,531		–1
	Educational	$ 5,819		–4
	Hospital & Health	6,218		–2
	Other Nonresidential Buildings	7,681		+ 1
	Total Institutional & Other	$ 19,718		–1
	Total Nonresidential Buildings	$ 58,249		–1

**1982 estimate includes $2.0 billion synthetic fuel plant

	Residential Buildings	1981 Actual	1982 Forecast	Percent Change 1982/81
Dwelling Units (thousands of units)	One-Family Houses	674		+19
	Multifamily Housing	450		+11
	Total Housekeeping Residential	1,124		+16
Floor Area (millions of square feet)	One-Family Houses	1,079		+19
	Multifamily Housing	478		+11
	Nonhousekeeping Residential	60		–8
	Total Residential Buildings	1,617		+15
Contract Value (millions of dollars)	One-Family Houses	$ 38,363		+29
	Multifamily Housing	17,821		+21
	Nonhousekeeping Residential	3,879		–2
	Total Residential Buildings	$ 60,063		+25
	Nonbuilding Construction			
Contract Value (millions of dollars)	Highways & Bridges	$ 11,126		–11
	Sewer & Water	7,677		+ 1
	Other Public Works	5,891		+ 7
	Total Public Works	$ 24,694		–3
	Utilities	$ 7,183		+25
	Total Nonbuilding Construction	$ 31,877		+ 4
	All Construction			
Contract Value (millions of dollars)	Total Construction	$150,189		+10
	Dodge Index (1977 = 100)	107		

Northeast

Connecticut, District of Columbia, Delaware, Massachusetts, Maryland, Maine, New Hampshire, New Jersey, New York, Eastern Pennsylvania, Rhode Island, Virginia, Vermont

Contract Value (millions of dollars)

	1981 Actual	1982 Forecast	Percent Change 1982/81
Nonresidential Buildings			
Commercial and Manufacturing	$ 7,489		–9
Institutional and Other	4,406		–8
Total	$11,895		–8
Residential Buildings			
One-Family Houses	$ 5,791		+26
Multifamily Housing	3,242		+18
Nonhousekeeping Residential	726		–4
Total	$ 9,759		+21
Nonbuilding Construction			
Highways and Bridges	$ 1,897		–6
Other Public Works	2,775		+10
Utilities	441		+ +
Total	$ 5,113		+14
Total Construction	$26,767		+7

South

Alabama, Arkansas, Florida, Georgia, Southern Illinois, Kansas, Louisiana, Mississippi, Missouri, North Carolina, Nebraska, Oklahoma, South Carolina, Tennessee, Texas

Contract Value (millions of dollars)

	1981 Actual	1982 Forecast	Percent Change 1982/81
Nonresidential Buildings			
Commercial and Manufacturing	$14,279		–7
Institutional and Other	6,900		–1
Total	$21,179		–5
Residential Buildings			
One-Family Houses	$17,043		+28
Multifamily Housing	6,996		+20
Nonhousekeeping Residential	1,552		–10
Total	$25,591		+24
Nonbuilding Construction			
Highways and Bridges	$ 4,275		–9
Other Public Works	4,563		+5
Utilities	*1,285		+63
Total	$10,123		+11
Total Construction	$56,893		+10

Midwest

Northern Illinois, Indiana, Iowa, Kentucky, Michigan, Minnesota, North Dakota, Ohio, Western Pennsylvania, South Dakota, Wisconsin, West Virginia

Contract Value (millions of dollars)

	1981 Actual	1982 Forecast	Percent Change 1982/81
Nonresidential Buildings			
Commercial and Manufacturing	$ 6,658		+29
Institutional & Other	4,281		–2
Total	$10,939		+17
Residential Buildings			
One-Family Houses	$ 5,956		+34
Multifamily Housing	2,773		+27
Nonhousekeeping Residential	549		+5
Total	$ 9,278		+30
Nonbuilding Construction			
Highways and Bridges	$ 2,854		–19
Other Public Works	2,699		+2
Utilities	1,475		+ +
Total	$ 7,028		+19
Total Construction	$27,245		+22

*1982 estimate includes $2.0 billion synthetic fuel plant

West

Alaska, Arizona, California, Colorado, Hawaii, Idaho, Montana, Nevada, New Mexico, Oregon, Utah, Washington, Wyoming

Contract Value (millions of dollars)

	1981 Actual	1982 Forecast	Percent Change 1982/81
Nonresidential Buildings			
Commercial and Manufacturing	$10,105		–8
Institutional & Other	4,131		+6
Total	$14,236		–4
Residential Buildings			
One-Family Houses	$ 9,573		+29
Multifamily Housing	4,810		+19
Nonhousekeeping Residential	1,052		+7
Total	$15,435		+25
Nonbuilding Construction			
Highways and Bridges	$ 2,100		–5
Other Public Works	3,531		–2
Utilities	3,982		–35
Total	$ 9,613		–16
Total Construction	$39,284		+4

+ + = Over 100% increase

If the mortgage rate reached by the end of 1982 remains resistant to upward pressures, the 1983 housing start total is tentatively estimated to be in the range of 1.5 to 1.6 million units.

Nonresidential Building

Contracting for nonresidential buildings held a strong and steady pace through 1981's deteriorating economic conditions, with quarterly index readings of 172-169-170-167 (1977 = 100). However, it took an unusual set of circumstances to accomplish what amounted to a remarkable balancing act.

In 1981, contracting for square footage of stores and shopping centers declined 9 percent, as would be expected in a housing crisis. Contracting for square footage of industrial building fell 14 percent, as would be expected in a business recession. Contracting for square footage of institutional building fell 12 percent, as would be expected in a squeeze on public spending. Yet in 1981, all of these across-the-board declines in nonresidential building were offset by a 30 percent gain in the booming market for offices. The lopsidedness of the nonresidential building market in 1981 is the key to its performance in 1982. Can office building continue to sustain this sector until the other categories begin to recover? How much life is left in the office boom? What are 1982 prospects for retail, industrial, and institutional buildings?

Offices The October 1981 edition of the *1982 Outlook* offered a more detailed analysis of the office building market than there is room for here. The main points were: 1) a rate of building in excess of 200 million square feet per year is not sustainable indefinitely (1981's total was 317 million); 2) a rate of building well above 200 million square feet has been needed for the past few years to reduce an accumulated backlog of demand resulting from extraordinary labor force growth in the late 1970's; and 3) this backlog has now been largely eliminated.

Two recent developments hint that the office boom may have peaked. The number of *large* office buildings being started dropped off sharply between the beginning and end of 1981, and the rate of *total* square footage started fell sharply in January 1982. Although severe weather may have been a factor in January's break, the prospect of a deeper recession supports the case for a decline of up to 21 percent this year.

Retail With almost all of 1982's housing recovery confined to the second half of the year, the derived demand for retail building that ultimately will be generated by an improved level of homebuilding will arrive too late in 1982 to prevent a decline of 6 percent. However, the potential for expansion in 1983 is good.

Manufacturing Lowered expectations for 1982 industrial production and capacity utilization translate into a later recovery and reduced volume of contracting for manufacturing buildings this year than previously expected. At an estimated 170 million square feet, the 1982 total will mark the third successive annual decline from 1979's peak of 243 million square feet.

Despite declining square footage, 1982 contract value of manufacturing building will be up significantly due to the start of the nation's first large-scale synthetic fuel plant in North Dakota. This $2.0 billion undertaking will not involve much square footage of enclosed structures in the conventional sense of industrial construction, however. Since this long-planned project obtained its Federal loan guarantee as recently as January 1982, it was *not* included in last October's *Outlook*.

Institutional Last October's estimate of a further modest decline in contracting for schools, hospitals, and other institutional buildings needs little adjustment at this time.

Commercial and industrial building, now estimated at only 800 million square feet in 1982, a 12 percent decline from 1981, nevertheless will exceed the volume of such building started in the 1975 recession by nearly 250 million square feet. Offices account for most of the difference.

Total nonresidential building in 1982 is now estimated at 1,040 million square feet for a value of $57.5 billion.

Nonbuilding Construction

Like almost all social programs, Federally funded construction has been cut in 1982. But unlike some, public works construction isn't bleeding badly, at least not yet. The 1982 contracting estimates for highways, mass transit, and other public works construction have been raised a bit, particularly in the area of sewer/water facilities, but still remain lower in total than 1981's actual value. Deeper cuts are coming, but the Administration's budgetary process has lost its early momentum. Congressional leaders, governors, and mayors are united in a chorus of protest against the President's New Federalism, holding out for a better balance of tax cuts and defense versus non-defense spending.

The 1982 estimate for utility construction, at $9.0 billion, remains unchanged from last October's forecast. From one to two billion dollars of this amount represents additional work on the Alcan gas pipeline.

Construction Market In Transition

By the end of 1982, economic forces will be leading the construction industry out of the transition it is now experiencing. With inflation beaten down and with recovery re-established, some of the basic priorities of Reaganomics will become more dominant: the shifting of Federal programs to local governments, and the trade-off between productive and military capital against social capital. These structural changes in our political and economic systems will greatly influence the direction of construction markets for many years ahead.

Prepared by the Economics Department, Mc Graw-Hill Information Systems Company

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The Outlook

Nonresidential Building Contract Value

Seasonally adjusted annual rates, in billions of dollars

Year	Quarter	Total	Commercial/ Industrial	Institutional
1981	I	$58.3	$37.8	$20.5
	II	57.6	38.9	18.7
	III	58.6	38.7	19.9
	IV	58.4	38.6	19.8
1982				
1981		$58.2	$38.5	$19.7
1982				
% Change		–1%	–1%	–1%

* Includes $2.0 billion synthetic fuel plant (annualized)

Residential Building Contract Value

Seasonally adjusted annual rates, in billions of dollars

Year	Quarter	Total	One Family	Multi-Family*
1981	I	$69.3	$46.0	$23.3
	II	62.7	41.3	21.4
	III	56.6	35.5	21.1
	IV	51.8	30.8	21.0
1982				
1981		$60.1	$38.4	$21.7
1982				
% Change		+25%	+29%	+16%

* Includes Nonhousekeeping Residential Buildings

Nonbuilding Construction Contract Value

Seasonally adjusted annual rates, in billions of dollars

Year	Quarter	Total	Public Works	Utilities
1981	I	$36.0	$27.6	$8.4
	II	35.3	22.4	12.9
	III	25.6	23.5	2.1
	IV	30.8	25.4	5.4
1982				
1981		$31.9	$24.7	$7.2
1982				
% Change		+4%	–3%	+25%

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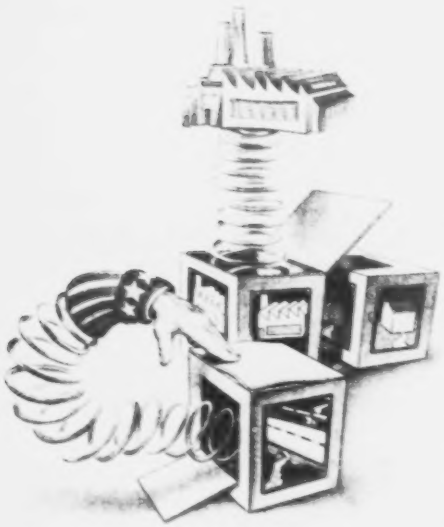

Is the wall that has been keeping the construction industry from breaking out of deep recession for the past year finally beginning to crumble?

Lower interest rates and a stronger economy are two prerequisites for the recovery of building activity. Both are good possibilities in the second half of 1982. (And better, still, in 1983.) A third helpful change, increased spending for trimmed-back public construction programs, remains in the realm of wishful thinking, however.

Two changes may be enough to make a difference.

Residential Building

The early 1980's will go down in building history as the triumph of monetarism over marriage. For the past three years (1980-82), the cumulative total of newly supplied shelter—some 3½ million conventionally built homes and apartments and another three-quarters of a million mobile homes—fell short of meeting even the most basic need created by the formation of some five million new households, much less replacing the loss of more than a million units from the existing stock of housing.

Conventional wisdom holds that with all this unmet demand piling up, there's nothing wrong with the housing market that a break in mortgage rates wouldn't cure overnight. It can't be denied that today's unrealistically high interest rates are the housing industry's most urgent problem. Yet, it is also true (and not quite so obvious) that important changes are taking place which will lead to different kinds of constraints once the current credit crisis has subsided. But that's another story.

For the rest of 1982 and 1983, no housing forecast is any better than the interest rate forecast upon which it is based. The most cogent argument for a decline of mortgage rates has less to do with the Federal Reserve and its restraint of the supply of credit than it does with the rate of inflation.

A 17 percent conventional mortgage rate (or its "creative equivalent") barely made sense when inflation was still in double digits, since the *real* rate of interest (nominal less inflation) was up in the range of 5 or 6 percent. With inflation now down to about 7 percent, the real rate of interest on a 17 percent mortgage is something like 10 percent! If 5 or 6 percent is the real rate of interest that is appropriate to the monetarist era, the addition of a 7 percent inflation factor means that 13 percent—not 17 percent—should be the equilibrium mortgage rate.

Getting there won't be easy, however. Interest rates are pegged to inflationary *expectations* more than they are to the *prevailing rate* of inflation, and the financial community (including the Fed) isn't convinced that 7 percent inflation is here to stay. The cause for doubt is the prospect of a series of $100 billion deficits which the Fed interprets as fuel for another round of double digit inflation once the economy recovers.

Under the "optimistic" assumption that lingering excess capacity throughout the economy will hold inflation to 7 percent for the next couple of years despite huge deficits, the conventional mortgage rate is projected to decline gradually from its peak of 17 percent at the start of 1982 to the range of 13 to 14 percent by the end of 1983. This "stickiness" of mortgage rates offers little opportunity for the recovery of housing starts in the rest of 1982.

With almost half the year's housing

activity already on the books at an average rate of less than a million dwelling units, 1982 begins to look like a replay of 1981—the industry's worst year in three decades. The President's veto of Sen. Lugar's $3 billion mortgage subsidy bill pretty well assures that it will be.

It's not likely that the defeated Lugar bill will be Congress' final attempt to provide homebuyers (and builders) some relief from current credit conditions. The odds are better than even that a substitute will surface before the November elections. Nevertheless, even a casual reading of the report of the President's Commission on Housing makes it clear that any housing aid program acceptable to the Reagan Administration would be one that did not require Federal outlays.

The mathematics of the housing market in 1982 requires that in order to reach a total of even 1.1 million units this year, the seasonally adjusted rate of housing starts must rise to 1.3 million by the fourth quarter. But without a significant decline in mortgage rates, and lacking the temporary help of mortgage subsidies, a jump to this rate of building in so short a time is not very likely. Under the conditions now assumed for 1982's second half, the fourth-quarter rate of building is more likely to be 1.2 million. This would leave the year's total somewhere above 1.05 million but short of 1.10 million units (and below 1981's total, as well).

Provided that a rate of 1.2 million units can be reached by 1982's final quarter, a steady decline of mortgage rates through 1983 would put a total of 1.4 million housing starts within reach next year.

Nonresidential Building

If the Reagan economic program were on schedule, commercial and industrial building would now be in the initial phase of a strong cyclical advance, responding to the multiple stimuli of tax cuts, accelerated depreciation, and deregulation. Instead, chronic recession has this volatile building market in the second stage of a decline that began in 1980.

The bottom of the commercial and industrial building cycle was probably reached at the middle of 1982 when contracting slid to a seasonally adjusted rate of 650 million square feet. Recovery from that point will depend on the timing and strength of the recovery of the economy as a whole; the normal lag of the commercial and industrial building cycle; and a special situation that applies to office building.

The stage is set for a recovery of the economy soon after midyear. The decline of GNP apparently ground to a halt in 1982's second quarter, and the $33 billion tax cut and a $12 billion hike in Social Security benefits scheduled for the third quarter are the ingredients of a widely anticipated advance in consumer spending. With inventory liquidation largely completed, spending gains should quickly be transmitted to production and employment. Only one thing stands in the way of the cumulative process that normally converts recovery into expansion: high interest rates. Because of this handicap, recovery from the recession of 1981/82 will not be all it could be.

Like most other forms of business capital spending, contracting for commercial and industrial building consistently lags general economic activity. One fea-

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Dodge Construction Potentials

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*1982 estimate includes $2.0 billion synthetic fuel plant

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**F. W. Dodge basis.

1982 Regional Estimates
Dodge Construction Potentials

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North-east

Connecticut, District of Columbia, Delaware, Massachusetts, Maryland, Maine, New Hampshire, New Jersey, New York, Eastern Pennsylvania, Rhode Island, Virginia, Vermont

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Total Construction	$26,767		-1

Mid-west

Northern Illinois, Indiana, Iowa, Kentucky, Michigan, Minnesota, North Dakota, Ohio, Western Pennsylvania, South Dakota, Wisconsin, West Virginia

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West

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Other Public Works	3,531		- 4
Utilities	3,982		-45
Total	$ 9,613		-17
Total Construction	$39,284		- 9

+ + = Over 100% increase

ture of this lag is a long, flat trough characteristic of the cycle once its decline has ended.

The place to look for the first sign of recovery of commercial and industrial building is in retail building, which is a derived demand of housing. As the housing market begins to recover in the second half of 1982, it would be reasonable to expect improvement in contracting for stores and warehouses early in 1983. But while 1983 offers the potential for recovery, 1982 will be the cyclical low point for retail building—an estimated 315 million square feet.

At the other end of the spectrum is manufacturing building—notoriously the last of the commercial and industrial building categories to respond to improving economic conditions. Capacity utilization is the critical factor that governs industrial building, and it will require the rest of 1982 and most of 1983 to absorb the excess capacity that currently abounds in the manufacturing sector. The bottom of the industrial building cycle will span both 1982 and 1983 at an average level of about 125 to 150 million square feet per year. The first significant gain (to above 175 million square feet) is

not expected until 1984.

Somewhere between the dependable cyclical behavior of retail building (the early cycle) and manufacturing building (the late one) lies the maverick of the commercial and industrial building group: offices.

As the result of an unprecedented boom which lasted all the way through 1981, office building was not only late in joining the recesssion but brought a surplus of unfinished buildings along with it. The price of having the unexpected support of office building in 1981, when most other building markets were falling apart, will be paid in 1983 when a moderate surplus of office space becomes a drag on recovery.

Bleak prospects for employment growth over the next eighteen months imply rising office vacancy rates, as last year's record volume of newly started projects becomes available for occupancy later this year. It is estimated that the cyclical adjustment to a temporary excess of office space, compounded by high unemployment, will bring the volume of office contracting down from its 1981 peak of 317 million square feet to 230 million in 1982, and down further in 1983 before turning up again in 1984.

Although the likelihood of further decline in the rate of total commercial and industrial building is small, recovery remains several quarters into the future as the normal lag of this market is extended by the aftereffects of an office boom that stayed too long. In 1982, it has to be enough that the long and steep decline of commercial and industrial building appears to have ended, and the conditions for recovery are taking hold.

Total nonresidential building, including both institutional and commercial/industrial building, now appears to be reaching its cyclical bottom in 1982 at 925 million square feet—a point that is astonishingly close to the low point of the mid-'70s cycle.

Nonbuilding Construction

One construction market that cannot anticipate a change in the circumstances that brought it down is public works. From a record $29 billion of contracting for highways and bridges, sewer and water facilities, and other public works construction in 1979, successive rounds of budgetary restraint have reduced the annual value of its contracting by 15 percent to its current $25 billion. After adjustment for inflation, public works construction is now only two-thirds its former peak volume.

The future of this construction market rests with the ability of state and local governments to provide additional funding for programs that the Federal Government is "retargeting" and "stretching out."

Budgeted outlays of the Federal Government in fiscal years 1982 and 1983 show an unchanged total of funding planned for public works programs at the reduced rate reached in the beginning of 1982. Meanwhile, state and local governments are exploring all possible sources of new revenue to cover shrinking Federal grants-in-aid. The promise of new and higher taxes in the future is little consolation in 1982, however, when the combination of recession and high interest rates are squeezing revenue and inhibiting bond sales.

In the short run, at least, this transfer of responsibility for public works construction from Federal to local government isn't working too well. The "best case" scenario is that contracting will increase enough to cover inflation (i.e., steady in constant dollars) for the next few years, until local governments are better adjusted to the New Federalism.

Transition to 1983

Two important changes in the environment for the depressed construction industry will be taking place in the second half of 1982. The economy will be working its way out of the on-and-off recession that has blighted two of the past three years. Interest rates should begin a downward adjustment to a more reasonable relationship with the rate of inflation. It would also be nice if public works programs were to be better funded—but two out of three are better than none.

Except for a barely noticeable improvement in housing starts by the end of the year, these events won't bring an immediate change in total construction contracting. What they will do is prepare the way for a better 1983 for the construction industry.

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The Outlook

Nonresidential Building Contract Value

Seasonally adjusted annual rates, in billions of dollars

Year	Quarter	Total	Commercial Industrial	Institutional
1981	I	$58.3	$37.8	$20.5
	II	57.6	38.9	18.7
	III	58.6	38.7	19.9
	IV	58.4	38.6	19.8
1982	I	$51.9	$32.2	$19.7
1981		$58.2	$38.5	$19.7
1982				
% Change		-7	-13	+4

* Includes $2.0 billion synthetic fuel plant (annualized)

Residential Building Contract Value

Seasonally adjusted annual rates, in billions of dollars

Year	Quarter	Total	One Family	Multi-Family*
1981	I	$69.3	$46.0	$23.3
	II	62.7	41.3	21.4
	III	56.6	35.5	21.1
	IV	51.8	30.8	21.0
1982	I	$54.0	$36.0	$18.0
1981		$60.1	$38.4	$21.7
1982				
% Change		+4	+7	—

* Includes Nonhousekeeping Residential Buildings

Nonbuilding Construction Contract Value

Seasonally adjusted annual rates, in billions of dollars

Year	Quarter	Total	Public Works	Utilities
1981	I	$36.0	$27.6	$ 8.4
	II	35.3	22.4	12.9
	III	25.6	23.5	2.1
	IV	30.8	25.4	5.4
1982	I	$37.6	$25.6	$12.0
1981		$31.9	$24.7	$ 7.2
1982				
% Change		+5	+1	+18